

**UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION**

ALLIANCE COMPANIES:)	Docket No. ER99-3144-009
)	
Ameren Corporation)	Docket No. EC99-80-009
American Electric Power Service Corporation)	
)	Docket No. RT01-88-001
Consumers Energy Company)	
Exelon Corporation)	
FirstEnergy Corp.)	
Illinois Power Company)	
Northern Indiana Public Service Company)	
The Dayton Power and Light Company)	
The Detroit Edison Company)	
Virginia Electric and Power Company)	

**MOTION TO INTERVENE AND PROTEST
OUT OF TIME OF THE STATE OF MICHIGAN
AND THE MICHIGAN PUBLIC SERVICE COMMISSION,
ILLINOIS COMMERCE COMMISSION,
MISSOURI PUBLIC SERVICE COMMISSION,
IOWA PUBLIC UTILITIES BOARD,
OHIO PUBLIC UTILITIES COMMISSION,
PENNSYLVANIA PUBLIC UTILITY COMMISSION,
INDIANA UTILITY REGULATORY COMMISSION
AND THE VIRGINIA STATE CORPORATION COMMISSION**

Pursuant to Rules 207, 212 and 214, the State of Michigan and the Michigan Public Service Commission, Illinois Commerce Commission, Missouri Public Service Commission, Iowa Public Utilities Board, Ohio Public Utilities Commission, Pennsylvania Public Utility Commission, Indiana Utility Regulatory Commission and the Virginia State Corporation Commission (hereinafter “State Commissions”) hereby request leave to intervene and protest out of time the Alliance Companies’ compliance filing of May 15, 2001 (“Compliance Filing” or “May 15 Filing”) in the above-captioned proceeding and urge the

Commission to order the relief requested herein. Persons on whom communications concerning this filing should be served are set forth in Appendix A. The State Commissions submit that good cause exists to accept their late-filed protests and interventions.¹

The State Commissions are committed to the goal of establishing a truly independent Regional Transmission Organization (“RTO”) which will provide buyers and sellers of electricity seamless access to a competitive market for electricity across a broad geographic region. Towards this objective, the State Commissions have been actively involved in the review of the relevant RTO compliance filings and the negotiation of the March 21, 2001 Settlement (“March 21 Settlement”) which creates the foundation of a seamless market across the Midwest RTO and the Alliance RTO.² The State Commissions have continued to work together in reviewing the instant filing to ensure full compliance with the Commission’s January 24, 2001 “Order On Compliance Filing and Providing Further Guidance,” *Alliance Cos.*, 94 FERC ¶ 61,070 (2001) (“January 24 Order”) and with the March 21 Settlement. The State Commissions have a substantial stake in the development of competitive wholesale and retail markets; indeed the success of retail competition is dependent on the existence of vibrant wholesale competition.³ Accordingly, the State Commissions have devoted substantial resources to the review process in this proceeding to assist the

¹ Most of the State Commissions joining this pleading have intervened in at least one of the above-designated dockets. To the extent they are not already intervenors, however, the State Commissions submit that good cause exists to allow their late interventions and joint protest. The instant filing is being submitted on June 18, 2001, the deadline originally set for intervention and protest and later shortened by the Commission. The State Commissions informed the Commission by letter, as soon as they discovered the comment period had been truncated, that it would not be possible to circulate a draft protest and obtain approval from all of the State Commissions participating in the short time then left. Moreover, since the Alliance Companies – the subjects of the protest – have consented to the late filing, no party is likely to be prejudiced by favorable Commission action on this motion, particularly at this stage of the proceedings.

² The March 21 Settlement was approved in *Illinois Power Co.*, 95 FERC ¶ 61,183 (2001).

³ As the State Commissions noted in their March 30, 2001 initial comments on the March 21 Settlement in Docket Nos. ER01-123 *et al.*, several state’s statutes will require the State Commissions to review, and approve or disapprove, certain requests by their jurisdictional utilities, such as a requests to transfer control of transmission assets to the Alliance. Nothing in these comments should be construed to suggest that the State Commissions have prejudged issues coming before them. They are instead reserving judgment until such time as the matters come before them in state proceedings.

Commission in reaching our common goals of a broad, seamless regional electricity market and a properly functioning, truly independent RTO.

SUMMARY OF COMMENTS AND PROTEST

Order No. 2000 sets December 15, 2001 as the deadline by which the Alliance RTO must be up and running. The Alliance Companies' May 15 compliance filing contains the required progress report, but little tangible evidence of progress itself. There is no managing member, no interim independent entity to facilitate the transition, no formal stakeholder process and no concrete plan for meeting the upcoming tariff filing milestones. The main goals of Order No. 2000 were independence and regionality, and Alliance is poised to achieve neither.

These results were not unforeseen. The March 21 Settlement approved by the Commission penalizes the Alliance Companies if the Alliance RTO is not operational by December 15, 2001. For every month beyond January 2002 that the Companies fail to meet the deadline, one month is shaved off the period during which the member companies will be able to charge a Zonal Transmission Adjustment.

The Alliance Companies have failed in numerous respects to comply with the Commission's January 24 Order in this proceeding and the Commission's subsequent May 8, 2001 Order on Rehearing, *Alliance Cos.*, 95 FERC ¶ 61,182 (2001) ("May 8 Order"). To date, they have failed to make material progress toward operational status, and in particular, have failed to propose a process for involving stakeholders in a formal and meaningful advisory role prior to formation of the RTO, or to take concrete steps to establish an entity independent of the transmission owners. The shortcomings in the stakeholder process are themselves symptomatic of the facts that there is still no independent entity with which stakeholders can collaborate and that the Alliance transmission owners ("Alliance TOs"), still in charge, have an inherent incentive to limit stakeholder input.

The need for a formal stakeholder advisory process is essential during the current period when crucial decisions are being made regarding formation of the RTO and where such decisions can limit the future options open to the RTO. Instead of taking steps to formalize and implement a Stakeholder Advisory Committee, the Alliance Companies have implemented a “top-down” process whereby critical issues, including the compliance actions required by the Commission’s January 24 Order and the March 21 Settlement, are unilaterally decided and announced by the Alliance Companies without the full benefit of stakeholder input. As a result, the State Commissions are left with no option other than filing protests, such as the instant filing, seeking Commission review of the Alliance Companies’ failure to comply with the January 24 Order, as well as the March 21 Settlement. The State Commissions are convinced that the public interest would have been better served if the issues raised in the Alliance Companies’ May 15, 2001 Compliance Filing had been subjected to collaborative review and resolution in the context of a formalized stakeholder advisory process. These issues, which are discussed in detail further below, include:

- (1) The failure to establish a formalized process for consideration of stakeholder input on key decisions related to formation of the RTO;
- (2) The failure to take steps to ensure Alliance RTO’s independence *prior* to the date it begins operation;
- (3) The failure to address the competitiveness of the market for energy imbalance and other generation-based ancillary services;
- (4) The failure to provide a detailed explanation of the terms of energy imbalance service;
- (5) The failure to provide sufficient details of the market monitoring program;
- (6) The failure to establish a process for acquiring goods and services;
- (7) The failure to provide an effective independence audit process; and
- (8) The failure to commence a stakeholder-inclusive process for addressing

congestion management, rate and other issues.

These failures should have consequences. The State Commissions urge the Commission to make clear to the Alliance Companies that to avoid penalties under the Settlement the RTO must be fully operational by December 15, 2001 not a skeletal entity that is an RTO in name only. It is not enough that the Alliance Companies be in nominal compliance with the Commission's January 24 Order at the various milestone dates (although, as discussed below, their May 15, 2001 filing falls short of even nominal compliance). The State Commissions emphasize, moreover, that "getting it right" is the priority, even if that results in some delay in the operational date of the RTO (and any resulting penalty). The State Commissions and other stakeholders should not be forced in future proceedings to undo the harm that would inevitably result from a hastily and poorly formed RTO.

Implicit in the requirement that an RTO meet the independence criterion of Order No. 2000 is that the companies forming it take interim steps to ensure the RTO's independence before it becomes operational. In other words, independence of operation requires independence in design. The Alliance Companies continue to fail this test because they have not taken the interim steps in their May 15, 2001 compliance filing to facilitate a transition to independence. The design process remains under the control of the Alliance Companies, most of whom are transmission owners having a stake in the success of their own generation investments. The absence of independence pervades the process: in the continued haze surrounding the search for a managing member, in the creation of a "BridgeCo" having no semblance of independence from the Alliance Companies, in the insistence on a confidentiality clause in Section 6.6 of the LLC Agreement which precludes state commissions (who may only have two representatives on the Advisory Committee) from cooperating in the same way the Alliance Companies have, and in the processes by which the Alliance buys goods and services and conducts audits of independence. The longer the delay

in turning the Alliance over to an independent managing member, the more likely that the design elements reflect the goals of transmission owners who also own generation. A distorted design will pose an insurmountable challenge to the eventual independent operator and its ability to create a functional, competitive wholesale market.

We discuss each of these points further below. However, the critical first steps toward independence are: (1) the creation of a formal stakeholder advisory process which provides all affected stakeholders, including State Commissions, with a meaningful opportunity to collaborate and provide input into the formation of the RTO prior to its operational date; and (2) that the Alliance Companies take immediate measures to form the Alliance LLC and, prior to its formation, take any other reasonable measures to ensure the independence of the RTO prior to its operation, such as the appointment of a majority non-owner transition board and staff to oversee RTO start-up and to interact with the formal stakeholder Advisory Committee that the State Commissions urge the Commission to establish.

I. Neither The Informal Stakeholder Advisory Process Now in Place Nor the Stakeholder Advisory Process Proposed to Take Effect Upon Operation of the Alliance RTO Comports with the Commission's January 24, 2001 Order.

The Alliance Companies assert that they have satisfied the Commission's directive to establish a stakeholder advisory process by establishing an informal process of consultation prior to the operational date of the Alliance RTO, to be replaced with a formal advisory committee pursuant to Section 6.6 of the Pro Forma Alliance Transco LLC Agreement included in their May 15 filing. As discussed in more detail below, the proposal fails in four basic respects. First, the advisory process is not the product of the collaboration with stakeholders expressly required by the Commission's January 24 Order in this case. Second, the "informal process" touted by the Alliance Companies is not an advisory process at all, but a top down process consisting of a highly programmed series of empty meetings at which the Alliance Companies

announce decisions, take attendance and schedule future meetings. Third, the informal “advisory” process violates the directive in the Commission’s January 24 Order and the March 21 Settlement to have an advisory process in place before the RTO operational date. Last, the formal advisory process that the Alliance Companies propose to implement when the RTO commences operations is itself flawed, precluding stakeholders from initiating meetings, burdening participants with unreasonable confidentiality restrictions and imposing no obligations on the RTO to give stakeholder advice serious consideration.

A. Both The Commission's January 24, 2001 Order and the March 21, 2001 Settlement Require the Alliance Companies to Design a Stakeholder Process “in Consultation with Stakeholders” and to Implement it Prior to RTO Formation.

The January 24 Order directed the Alliance Companies to develop an advisory process in consultation with stakeholders, to describe that advisory process and identify the participants. *Alliance Cos.*, 94 FERC at 61,304. Section 3.3 of the March 21 Settlement agreement similarly provides that “the Alliance Companies, *in consultation with stakeholders*, shall establish a process for securing on-going stakeholder involvement in the Alliance RTO” and that “the process will be proposed to the Commission no later than May 15, 2001.” (Emphasis added). Section 3.3, moreover, makes clear that the process is to begin *before* RTO formation: “The purpose of the stakeholder process will be to provide a forum(s) for stakeholders to provide *on-going* advice to the Alliance Companies and, in turn, upon its creation, the Alliance RTO.” (Emphasis added). The Alliance Companies’ compliance filing does not satisfy this obligation.

1. The Stakeholder Advisory Process Was Not the Product of Collaboration with Stakeholders.

The directive to the Alliance Companies to develop a meaningful stakeholder process has its origin in earlier disputes between the Alliance Companies and stakeholders. One of the most contentious – unnecessarily contentious – issues surrounding the formation of the Alliance RTO has been stakeholder input. The January 24 Order identified inappropriate limits, placed by the Alliance Companies, on stakeholders’ ability to have input, and found:

The processes that stakeholders can use to communicate and consult with an RTO should be developed in consultation with stakeholders. *If RTOs are to be responsive to the needs of the market, there must be a meaningful and efficient process for communication and consultation that serves not only the needs of the RTO, but also the needs of the stakeholders.* We believe that requiring Alliance to unilaterally propose these processes and having the Commission direct changes in processes based on the comments of stakeholders is not the best way to develop workable processes for stakeholder communication and consultation. We believe that a better approach is for the Alliance Companies to develop an advisory process in consultation with stakeholders, and to describe that advisory process and identify the participants. Only if they cannot will the Commission step in.

Alliance Cos., 94 FERC at 61,304 (emphasis added).

This issue also figured prominently in the subsequent Midwest ISO (“MISO”)/Alliance Settlement and in the Commission’s May 8 Order Denying Rehearing:

Midwest Customers also ask that we clarify that future proposals regarding congestion management and other issues, be developed in consultation with stakeholders. In the *Alliance III Order* we specifically stated that requiring Alliance to unilaterally propose stakeholder processes was not the best way to develop workable processes for stakeholder communication and consultation. [Footnote omitted.] Due to recent events, we see no need to provide the clarification requested by Midwest Customers. We note that since the Alliance III Order issued, Alliance Companies have been actively engaged in the stakeholder process and have already held stakeholder meetings on such topics as congestion management, and plan to hold more meetings in the near future on other issues (e.g., generator interconnect procedures). In addition, Section 3.3 of the Settlement provides that Alliance Companies will implement a process for securing *on-going* stakeholder involvement

in the Alliance and will file such a process with the Commission. Therefore, Midwest

Customers will have an opportunity to comment on the stakeholder process at that time.

Alliance Cos., 95 FERC at 61,637 (emphasis added).

Neither Section 6.6 of the Pro Forma Agreement nor the informal stakeholder advisory process described in the May 15 Compliance Filing were the product of collaboration with stakeholders. Thus, the Alliance Companies, by definition, have not complied with the spirit, much less the letter, of the January 24 and May 8 Orders or Section 3.3 of the Settlement. Despite being told twice by the Commission to develop, *collaboratively* with affected stakeholders, procedures for obtaining stakeholder input, the Applicants are proposing the same basic procedures as before, leaving it to the stakeholders yet again to argue that they are insufficient, and the Commission to decide the issue yet again. This is exactly what the Commission told the Alliance Companies it did not wish to do.

2. The Informal Stakeholder Advisory Process Described by the Alliance Companies Does Not Provide Opportunities for Meaningful Stakeholder Input and Involvement.

The Alliance Companies' failure to collaborate on the development of an advisory process, while violative of the Commission's Orders, would nonetheless have been inconsequential had the process, even if unilaterally developed, been meaningful. Unfortunately, that has not been the case. While the Commission correctly recounted the Alliance Companies' statements that a substantial number of stakeholder meetings have occurred since the filing of the Settlement, meetings in and of themselves do not an effective stakeholder process make. That the Alliance Companies cite only the meetings, and not their results, makes the point well. The Alliance Companies' idea of a consultative process is to go through the motions: schedule a meeting, set an agenda, make a series of Powerpoint presentations, ask for questions and comments from stakeholders, and listen to the resulting discussion (which at certain meetings has been quite vociferous). Decisions are made in closed meetings by the Alliance Management Committee (composed of

one representative from each Alliance TO, or another such decision-making group unknown to the stakeholders. At some point decisions are simply relayed back to stakeholders. Poor communication (such as short notice of meetings and discussion topics, and failure to distribute in advance sufficiently detailed materials on topics to be discussed) has also been a problem.

On a more substantive level, customer representatives have had little real opportunity to interact with the actual decision makers among the Alliance Companies, and do not even know if the concerns and feedback they have expressed at stakeholder meetings have been conveyed fully and accurately to those decision makers.⁴ Examples of these problems highlight their seriousness.

3. Meetings to Discuss Energy Imbalance and Congestion Management.

Illustrating well the deficiencies in the Alliance Companies' informal advisory process is the series of Market Development Advisory Group ("MDAG") meetings held in Baltimore in April, May and June of this year. In their Transmittal Letter to the May 15 Compliance Filing (at 10), the Alliance Companies state that this group "continues to meet on a bi-weekly basis and is actively involved in discussions related to market-design approaches to energy imbalance and congestion management." That much is true. But the Commission should not misapprehend these discussions as collaborative, or infer significant stakeholder input into the development of energy imbalance and congestion management approaches.

In fact, the opposite is true. The Alliance Companies' representatives and their consultants set the agendas, make the vast bulk of the presentations, answer questions from the stakeholder representatives regarding the topic of the hour, leave many other questions unanswered, and resist efforts to open up the

⁴ It does bear noting that joint meetings with neighboring RTOs, such as the MISO, seem to have a tempering effect on the Alliance's attitude toward stakeholder input. The June 7-8, 2001 Alliance/MISO Stakeholder Meeting in Rosemont, Illinois was a marked improvement over prior meetings between the Alliance Companies and stakeholders. It involved a two day meeting to consider line by line comments from generators and others on a 115 page joint MISO/Alliance Interconnection Agreement that had been circulated to stakeholders about a week before the meeting.

process to make it fully collaborative. At virtually every MDAG meeting to date, stakeholders have attempted to give the MDAG a more formal structure or develop a direct relationship with the Alliance TOs' Management Committee, only to be rebuffed repeatedly. Efforts to put topics on the table that the Alliance Companies do not wish to discuss (*e.g.*, potential market power in the Day One Energy Imbalance market) have met with rejection. At the June 5 MDAG Meeting, one Alliance TO representative reiterated in no uncertain terms that the MDAG was indeed only an advisory group, that neither the Management Committee (nor the Managing Member once selected) was bound in any way to adhere to the MDAG's decisions, and that the participating stakeholders should not assume that they have any decision-making authority.

As a result, those parties expending the considerable resources necessary to attend these meetings have no clear idea of how their opinions and concerns are being conveyed back to the Management Committee, other than the assurances of the official Management Committee Liaison to the MDAG that these concerns are indeed being conveyed. This problem is exacerbated because at the present time, it is the Alliance Companies' Management Committee – rather than the staff of the yet-to-be formed Alliance RTO – that is making the important policy decisions. As long as this is so, many participants lack faith that these decisions are being made in the best interests of markets and consumers.

The twin concerns of the lack of a truly collaborative process and the lack of independent RTO decision making has led some state commissions to conclude that it simply is not a worthwhile use of their scarce personnel and resources to send representatives to MDAG meetings. This rational judgment, in turn, has skewed the universe of participants attending the meetings, so that transmission owner and generator representatives (and their viewpoints) dominate them. Such a decision to refrain from participation,

however, carries its own Hobson's Choice. The Applicants are then free to argue that stakeholder representatives have failed to participate and their views should therefore be discounted.

The above-noted concerns with the Alliance Companies' stakeholder processes are nothing new. State Commission representatives have had them for many months, which is one reason why Section 3.3 of the Alliance/MISO Settlement was included in the settlement document in the first instance. Nor are they news to the Alliance Companies, who have been made well aware of them by State Commission representatives. Nor is there anything new about the Alliance Companies' continuing response: plenty of process, but minimal substance.

The Alliance Companies cannot have it both ways. Either they must make the advisory committee process meaningful for the stakeholders, by giving the stakeholders a real opportunity to raise their concerns to the RTO's decision makers and ceding decision making to an independent RTO at the earliest possible moment, or they must acknowledge to the Commission that they are not doing so. Unfortunately, the May 15 Compliance Filing leaves this point vague, describing the MDAG as being "actively involved in discussions," and having "begun work on a number of issues." Transmittal Letter at 8, 10. The State Commissions are concerned that at later stages of this proceeding, the Alliance Companies will attempt to use the fact that numerous such meetings were held to justify whatever proposals the Alliance Companies choose to file unilaterally. The Commission should labor under no illusion that the MDAG and other such groups are anything but nominally advisory in nature, and that the proposed policies and procedures that the Alliance Companies may file are anything but their own unilateral proposals.

B. A Formal Stakeholder Process Must Be Implemented Before the RTO Becomes Operational. It Should Take the Form of a Revised Section 6.6 of the Pro Forma Agreement.

If the Commission wishes the current situation to change, it is going to have to instruct the Alliance Companies directly to alter their current course of action to accommodate a truly collaborative stakeholder process. Specifically, the State Commissions urge the Commission to direct the Alliance Companies to establish a formal process under which stakeholders, as well as the Alliance Companies, can fully participate.

The Coalition of Midwest Transmission Customers and Public Interest Organizations (“Midwest Stakeholders”), like the State Commissions, has urged the Commission to require the Alliance Companies to adopt a formal advisory process in advance of the RTO’s operational date. They have suggested that, with certain modifications, the Commission could order the Alliance Companies to implement immediately the formal advisory process that they have only proposed to take effect when the RTO commences operation. The State Commissions agree with the modifications the Midwest Stakeholders have suggested to Section 6.6 and, for clarity, we repeat them here:

First, language that permits the managing member, in its sole discretion, to modify the Advisory Committee has been deleted. Permitting the manager member to have this sole discretion could circumvent the objective to have the Advisory Committee provide a balanced representation of stakeholders. As written, this language would suggest that the managing member’s discretion would not be subject to any Commission review or approval.

Second, the requirement for Advisory Committee participants to execute a confidentiality agreement of undefined scope as a condition of participation in any meeting has been deleted. This requirement is unnecessary and highly onerous and Joint Midwest Intervenor know of no similar restrictions in any existing RTO or ISO advisory framework.

Third, language has been added to permit the Advisory Committee to determine the

frequency of meetings, and language that restricts the Advisory Committee to quarterly meetings has been deleted. The Advisory Committee should be able to meet as often as is necessary to conduct its required business.

Fourth, membership on the Advisory Committee has been modified to reflect participation by two external border RTOs, rather than two external border transmission owners (which may or may not be RTOs). Given the requirement in Order 2000 for interregional coordination, and obligations under the IRCA, participation by border RTOs is more appropriate than participation by external border transmission owners.

Finally, the term stakeholder has been substituted for the term customer in a number of places throughout Appendix I. Many of the designated participants in the Advisory Committee, such as state regulatory commissions, would not be customers of Alliance Transco. Thus, the term stakeholder has been substituted for clarity.

Motion to Intervene and Protest of the Coalition of Midwest Transmission Customers and Public Interest Organizations, Docket Nos. RT01-88, *et al.* at 16 (June 13, 2001).

The confidentiality restriction discussed above is particularly troublesome. The Commission's January 24 Order stated:

Under Alliance Companies' proposal, stakeholders are limited in their ability to consult with each other as part of the stakeholder input process and are potentially subject to confidentiality requirements, in that Alliance will control all aspects of membership eligibility, voting, and the formation of new stakeholder groups, and due to the Alliance Companies' proposal to limit stakeholder communications through mandated confidentiality agreements. . . . If RTOs are going to be responsive to the needs of the market, there must be a meaningful and efficient process for communication and consultation that serves not only the needs of the RTO, but also the needs of the stakeholders.

Alliance Cos., 94 FERC at 61,304.

In their May 15 Compliance Filing (at 10-11), the Alliance Companies state that Section 6.6 of the LLC Agreement "has been revised to clarify that customers may openly consult with one another as part of the customer advisory process." They made this revision, presumably, because a confidentiality requirement would conflict with an efficient stakeholder input and communication process.

Review of the revised Section 6.6 of the LLC Agreement (Attachment D), however, reveals that it has not been revised. Section 6.6 (c) still states:

A Committee Representative shall not be entitled to participate in meetings or receive information regarding the Company until such Committee Representatives shall have executed and delivered a confidentiality agreement in form and substance satisfactory to the Managing Member.

As such, Section 6.6(c) of the LLC Agreement still would require representatives on the Advisory Committee to sign a confidentiality agreement of unknown scope. State Commission representatives on the Committee could not carry out their public interest duties or their responsibilities to their fellow commissions (that is, commissions affected by Alliance initiatives but not directly represented on the Committee) if required to sign an onerous confidentiality agreement. As it stands, the proposed unbounded confidentiality requirement would undermine the Advisory Committee's efficacy.

Because of the Alliance Companies' failure to address this matter, the State Commissions request that the Commission do so, by striking Section 6.6(c) of the LLC Agreement. This action would be consistent with the Commission's prior guidance and with the Alliance Companies' own avowed intentions to permit customers to "openly consult with one another as part of the customer advisory process." Transmittal Letter at 11.

In addition to the modifications to Section 6.6 urged by the Midwest Stakeholders, the State Commissions also urge the Commission to direct the Alliance Companies to establish a process under which stakeholders, as well as the Alliance Companies, can call meetings and vote to include agenda items. To make this process meaningful, the Commission should require the Alliance Companies to commit qualified personnel involved in the stakeholder process to participate not just on issues on the Alliance Companies' agenda, but to participate on committees and task forces that the stakeholders may elect to create. Finally,

to ensure that the Alliance Companies are not merely paying lip service to stakeholder involvement, the Commission should require the Alliance Companies to explain in writing any decision to reject a proposal properly introduced to the Advisory Committee and supported by a majority of the stakeholders participating. This requirement will not make adoption of the Advisory Committee recommendations mandatory, but it will make it more difficult for the Alliance Companies to reject the stakeholders' recommendations arbitrarily.

II. The Absence of a Meaningful Stakeholder Process, Coupled With the Alliance Companies' Failure to Take Interim Steps To Establish Pre-Operation Independence for the Alliance RTO, Has Impeded Progress Towards Commencement of Independent RTO Operations.

A. The Alliance Companies Are Required, but Have Failed, to Take Timely Interim Steps to Establish the Independence of the Alliance RTO before it Becomes Operational.

Whether the Alliance Companies' May 15, 2001 compliance filing meets the requirements of the Commission's January 24 Order depends, at least in part, on whether their latest compliance effort fulfills other obligations previously undertaken. One obligation previously assumed by the Alliance Companies, but not reflected in the May 15, 2001 filing, was the agreement to create an Alliance ISO to be in operation until formation of the Alliance Transco. That obligation, which would help ensure a measure of essential pre-operational independence for the RTO, has not been satisfied. The failure to satisfy that condition, in turn, has left establishment of a collaborative process entirely in the hands of the existing, reluctant Alliance transmission owners. Not surprisingly, as has been discussed, *supra*, a true collaborative process has not been established. It is unfortunate, but also no surprise, to discover that progress toward full RTO operation has been halting and slow. The absence of independence and the absence of a meaningful stakeholder process have worked together to produce these unsatisfactory and unacceptable results.

The State Commissions wish to be clear. Our dissatisfaction with the progress toward independence is not a simple gripe and a wish. The Alliance Companies' failure to take steps to establish a measure of pre-operational independence for the RTO is an issue of non-compliance with their own promises and the Commission's directives and is within the Commission's authority to remedy in this proceeding.

On June 3, 1999, the Alliance Companies filed an application under Section 203 of the Federal Power Act ("FPA") seeking the authority for "transfer of control over operations of jurisdictional transmission facilities owned by the Alliance Companies to the Alliance Independent Transmission System Operator, Inc. (Alliance ISO)" as an interim step preceding transfer of control to the Alliance Transco. The Alliance Transco, the Companies maintained, would qualify as an RTO under the Commission's then extant RTO NOPR. *See Alliance Cos.*, 89 FERC ¶ 61,298 at 61,915 (1999). In addition, in Docket No. ER99-3144, the Alliance Companies submitted for filing under FPA Section 205 an agreement establishing the Alliance ISO and the Alliance Transmission Co. *Id.*

As originally proposed, the Alliance Companies stated that they would declare their intentions to transfer ownership of their transmission facilities to the Alliance Transco within 90 days of a Commission order approving the transfer. Importantly here, if the declarations from member companies did not signify intentions by at least one owner with \$1 billion in transmission assets to divest ownership, the Alliance Companies agreed to "create the Alliance ISO." *Id.* at 61,916. This entity was to "continue in operation until one or more of the Alliance Companies triggers the transition from the Alliance ISO to the Alliance Transco." *Id.*

In addressing the pre-Order 2000 filing by the Alliance Companies, the Commission stated that the proposed Alliance Transco would not meet the independence criteria of Order No. 888 and therefore,

would fall short of the independence requirements of the RTO NOPR as well. *Id.* at 61,919. On the other hand, the Commission did find that, with some modifications, the governance structure of the Alliance ISO “would meet the Commission’s ISO Principle No. 1 [independence].” *Id.* One of those modifications underscored the Commission’s concern that independence could not be achieved magically on the date operation of an ISO or RTO commenced, but required interim protections as well. Among other things, the Alliance proposal would have allowed the initial ISO Board to be selected exclusively by the Alliance Companies. The Commission ruled that such a restriction would compromise the ISO’s independence. *Id.*

The requisite declarations did not take place within 90 days of the Commission’s December 20, 1999 Order,⁵ but the Alliance Companies did not take the steps promised to “create the Alliance ISO.” *Alliance Cos.*, 89 FERC at 61,916.⁶ The unfortunate result is that there is no independent entity controlling transmission in the interim before the Alliance RTO begins operation. The State Commissions recognize that, as a practical matter, an ISO cannot now be created prior to RTO formation. But the Commission can and should direct the Alliance Companies to take other, comparable measures to ensure independence of the RTO now, and not just subsequent to its operation, such as requiring the establishment of an

⁵ FirstEnergy did file, in 1999, to transfer its transmission assets, with a net book value of \$662 million, to the American Transmission Company, but it did not claim that such a transfer constituted a declaration to transfer those facilities to the Alliance Transco, *FirstEnergy Operating Cos.*, 89 FERC ¶ 61,090 at 61,256 (1999), nor did other Alliance members make declarations regarding transfer within the 90 day period.

⁶ In their June 13, 2000 letter to the Commission, the Alliance Companies stated that they did “not anticipate that the Alliance ISO will be created because one or more of the Alliance Companies intends to propose to trigger the conditions under which the Alliance RTO would begin operations as a for-profit transmission company – the Alliance Transco.” September 15, 2000 letter from Alliance to the Commission at 8, n.18 (citing letter of June 13, 2000). The basis for this assertion is unclear, since the June 13th letter itself came well after the trigger date for the Alliance Companies to announce their divestiture intentions and to begin creation of an Alliance ISO. The Alliance Companies’ assertion may have been based on the conclusion, asserted in their February 17, 2000 compliance filing, that the Commission’s December 20, 1999 Order was insufficiently “definitive” and did not constitute the “Required Regulatory Approval” that would have triggered the 90 day clock. See February 17, 2000 Compliance Filing of the Alliance Companies, Docket Nos. ER99-3144 and EC99-80, Transmittal Letter at 17. The Alliance Companies later appeared to have abandoned this position, recounting in their January 15, 2001 compliance filing that, as late as September, 2000, they had submitted modifications to the ISO Bylaws required by the Commission’s May 18, 2000 Order, *Alliance Cos.*, 91 FERC ¶ 61,152 at 61,569 (2000).

independent BridgeCo (*see infra*) or the appointment of a majority non-owner transition board to oversee RTO start up and to interact with the stakeholder Advisory Committee as the State Commissions have already urged the Commission to do. The consequences of the Alliance Companies' failure to establish an interim independent decision maker or a true collaborative stakeholder advisory process are discussed in the succeeding sections.

B. The Alliance Companies Need, but Lack, Concrete Plans for Creating an Independent Managing Member.

The Alliance RTO cannot become independent without an independent managing member. Yet there is no clear deadline for when a managing member will be in place, and the Alliance Companies' plans for making this happen have become hazy.

In their January 16, 2001 filing in RT01-88 ("January 16 Filing"), the Alliance Companies revealed plans to abandon their proposal to create the Alliance Managing Member through an Initial Public Offering ("IPO"), a method which the Commission previously had approved. Instead they described two broad alternatives for finding a managing member: (1) attracting a "strategic investor;" and (2) attracting "financial-only investors." January 16 Filing at 13-14.

In contrast, the May 15 Compliance Filing included no discussion on either of these alternative methods. This omission is problematic, since the May 15 Filing purports to "supplement[] the initial filing submitted in compliance with Order No. 2000 on January 16, 2001." May 15 Filing at 1. Reflecting and perhaps increasing this uncertainty is the status of the apparent negotiations between the Alliance Companies and National Grid USA ("National Grid") over whether the latter would become the Managing Member. *See* National Grid Petition for Declaratory Order, Docket EL01-80-000 (requesting a ruling that National

Alliance Companies' September 15, 2000 Compliance Filing, Transmittal Letter at 12, n.13. There, the Companies simply

Grid is not a “market participant” under Order No. 2000). Without meaning to indicate support or disapproval for National Grid’s request, we would expect substantial questions to arise as to whether National Grid’s undisputed role as a market participant in regions proximate to the Alliance Companies will pose difficulties to its designation as a non-market participant in the Alliance region. In particular, National Grid’s role as a market participant in nearby regions could influence its judgments as to whether to expand the Alliance’s boundaries and whether and how to address seams with those regions.

Ongoing uncertainty concerning the selection of an independent managing member disserves the public. It slows the crucial process of moving the Alliance from an alliance of generation owners using their transmission assets to serve their individual generation strategies, to an independently managed regional transmission entity. During this interim period, meanwhile, decisions with long-lasting effect are emanating from a process dominated by transmission-owning generation members. The Commission therefore should: (1) address in this docket the appropriateness of the Alliance’s two new concepts; and (2) expedite its ruling on National Grid’s request.

There should have been a Managing Member in place long ago, but the State Commissions recognize that the facts on the ground dictate the possible. The Commission should therefore establish a deadline for getting the Managing Member in place and turning over to it all further RTO development decision-making from the vertically-integrated Alliance Companies as soon as practicable. The Commission should further require that the Managing Member review all prior decisions made by the Alliance transmission owners and, to the extent they deem necessary, alter those decisions. We recommend a Commission deadline of September 1, 2001. Nothing in previous Alliance Companies’ submissions, including the Limited Liability Company Agreement of Alliance Transmission Company, LLC (included as

announced, without explanation or request for approval, that they did “not intend to form the Alliance ISO.” *Id.*

Attachment K to the September 15, 2000 filing) precludes establishing the Managing Member before the RTO operational date.

C. The “BridgeCo” Announcement Does not Solve the Problem of Independence, and May Exacerbate It.

Through a press release issued March 28, 2001, the Alliance Companies announced the creation of a “special purpose organization,” named “BridgeCo,” to “manage the transition to the independent Alliance Transmission Company.” Specifically:

The interim entity will facilitate the process leading to the operation of the Alliance Transmission Company, including management of various vendor contracts for operational implementation, and providing a vehicle to attract independent investors. It will provide a more formal process for the development of an organization that will independently operate, and could own, the transmission systems of the Alliance companies.

Press Release at 2.

There is no doubt that the Alliance Companies have to move swiftly to implement Order No. 2000. But the BridgeCo decision, by itself, does not accord with the Commission’s goals, for several reasons.

First, BridgeCo operates outside of the procedures that the parties, stakeholders and the Commission have established for airing Alliance issues. It appears nowhere in the Alliance Companies’ May 15 Filing, even though the May 15 Filing purports to “supplement[]” its January 16 Filing. May 15 Filing at 1. Moreover, despite much talk about a stakeholder process, the Alliance Companies engaged in no consultation with stakeholders before creating, staffing and instructing BridgeCo.

Second, BridgeCo cannot stake any claim to independence. BridgeCo is a creature of the Alliance Companies, dependent on them for resources. It is the State Commissions’ understanding that BridgeCo’s new CEO was hired by the Alliance Companies, and its staff are on loan from the Alliance Companies.

This is not a recipe for independence. At the present time, the Alliance Companies' strategic goal appears to be to use BridgeCo to their maximum strategic advantage, laying as much concrete as possible until an independent managing member arises.

Third, the BridgeCo will be laying the foundation for future Alliance operations. This foundation will both drive and limit future decisions. If this foundation reflects only the wishes of the generation-owning transmission owners who created BridgeCo, there will not be a seamless Midwest market. Future suggestions from others could be rejected by Alliance Companies, or even the new independent RTO, on the grounds that the concrete has hardened and it would be simply too expensive to start over.

The Commission must move BridgeCo in the right direction. If BridgeCo is going to "manage the transition to the independent Alliance Transmission Company," it should itself be an independent entity.

The State Commissions recognize the reality that the Alliance Companies do not yet have a Managing Member and that one may not be found for some time. The Commission cannot remain passive about the consequences, however. The May 15 Filing says nothing about the form of the BridgeCo. What will be its structure? Will it take the form of a temporary ISO? Will it have a disinterested manager, an independent staff, sufficient funding? Will it share information with stakeholders? Unless the Commission demands answers it will be impossible to tell if the BridgeCo will facilitate a transition to independence and, as important, whether it can do so on a sufficiently timely basis to assure affected stakeholders that the process has not been skewed toward a structure that will favor the Alliance owners once the RTO becomes operational. "An RTO," the Commission stated in Order No. 2000, "must be independent in reality and perception." FERC Stats. & Regs. ¶ 31,089 at 31,061 (1999). At this point, Alliance is neither, and its member companies have to this point given nothing but lip service to the Commission's aspirational admonition. Unless the Alliance Companies can offer assurance that the BridgeCo itself will be independent

of the transmission owners, the dangers described above will remain, as will the perception, if not the reality, that the RTO formation process has been compromised.

The State Commissions urge the Commission to direct Alliance to provide the details discussed above and to demonstrate that the BridgeCo will be independent of the Alliance Companies in the fullest practical sense. The Commission should further direct the Alliance Companies to take these steps promptly.

D. The Lack of Independence and a True Stakeholder Process Have Slowed Development of a Market Monitoring Plan.

The January 24 Order criticized the Alliance Companies' market monitoring proposal as "lack[ing] sufficient details." Specifically,

While Alliance Companies have outlined the broad structure of the market monitoring program and the market monitor's duties, the proposal fails to explain how the program will actually function and how the market monitor will perform its duties.

Alliance Cos., 94 FERC at 61,317. The Order required the Alliance Companies to resubmit their market monitoring plan, with more details and with an explanation of the scope of the market monitor's authority.

Id. The Companies also were "to meet with interested parties to craft a plan" *Id.*

In the May 15 Filing, the Alliance Companies submitted details concerning their compliance with Article VIII of the IRCA. That provision provides that Alliance and the Midwest ISO would hire an independent market monitor ("IMM") and establish a Market Monitoring Committee. The IMM is supposed to analyze activities and events, recommend efficiencies and improvements, file periodic reports with the Commission and other agencies and will determine whether any markets administered separately by the Alliance RTO and the Midwest ISO are compatible as required by the IRCA.

Contrary to the requirements of the January 24 Order, the Alliance Companies have not involved the stakeholders meaningfully in the coordination process with MISO. Instead, the Alliance Companies, MISO and the Southwest Power Pool have unilaterally announced the selection of Potomac Economics as their joint IMM. This may be a sound choice, but on its face it underscores the State Commissions' concerns about the absence of a true stakeholder process. David Patton, identified by MISO as the "principal economist" for the IMM, was a consultant for the Alliance Companies on the central issues of transmission pricing and RTO scope. His selection creates at least the appearance of a dependent, rather than independent relationship between the IMM and the Alliance transmission owners.

III. The Alliance Companies Have Left Too Many Compliance Items for Later

A. Introduction

Assuming a proposed operations date of December 15, 2001, the Alliance Companies must satisfy all additional compliance matters by August 17, 2001. The actual tariff rates, terms and conditions must be filed "no later than 120 days prior to the commencement of operations." *Alliance Cos.*, 94 FERC at 61,302, 61,329. Full compliance with prior Commission orders requires clear commitments and detailed plans for resolving numerous outstanding issues such as rates, scheduling and security coordination.

The May 15 filing contains entirely too many examples of "details to come later." A compliance filing should demonstrate compliance. This filing does not. As December 15 looms ever closer, and myriad details of the Alliance RTO proposal remain undecided, it will grow more and more difficult for the Commission, State Commissions, and other intervenors to review the remaining aspects of the proposal meaningfully. As discussed further in this section, many compliance items still outstanding are issues of great significance, including the following:

?? Ancillary Services: The compliance filing does not provide adequate details about the

proposed energy imbalance market; nor does it address concerns regarding the adequacy of competition in the ancillary services market.

- ?? OASIS and Total Transmission Capability: The compliance filing's revisions to the Operating Protocol still lack detail, and are contingent on proper implementation of the IRCA process, about which the May 15 filing says very little.
- ?? Market Monitoring: This aspect of the compliance filing is inchoate, and depends on what is done in the IRCA implementation process.
- ?? Rate Issues: Despite directives in the Commission's January 24 Order, the compliance filing does not address various rate issues; rather, it defers these issues to filing(s) to be submitted no later than 120 days before the service date.
- ?? Non-Rate Terms and Conditions: The compliance filing treats these the same as it does the rate issues.
- ?? Corporate Formation Documents: The Alliance Companies have yet to file the final corporate formation documents, in either draft or final form.

Because of the many holes left in the compliance fabric, and the shortness of time, the Commission should not allow the Alliance Companies to defer until their August tariff filing compliance with the many outstanding items they should have addressed in the May 15 Compliance Filing. The Alliance Companies should be required to file a supplemental compliance filing on an expedited basis to address the shortcomings in their May 15 Compliance Filing.

B. The Alliance Companies Have Failed to Address, Much Less Demonstrate the Competitiveness of the Ancillary Services Market. This Problem Has Been Exacerbated by the Absence of a Meaningful Stakeholder Process.

1. Energy Imbalance Service.

The Alliance Companies are proposing that the Alliance RTO use a market-based approach to provide generation-based ancillary services. For example, they propose to have the RTO employ a market-based approach to provide Energy Imbalance Service on Day One of RTO operations (presently set for December 15, 2001).

A number of parties protested the Alliance Companies' proposed method of supplying Energy Imbalance Service at earlier stages of this proceeding and have continued, without success to attempt to have the issue considered in the so-called advisory process discussed at length earlier. On this subject, the Commission's January 24 Order found:

Alliance Companies' proposal lacks sufficient details. Intervenors have raised a number of concerns regarding the operation of the proposed energy imbalance market and we direct Alliance Companies to address these concerns when they make their compliance filing to this order. *For example, Alliance Companies should address concerns regarding the adequacy of competition in the market.* Alliance Companies should also explain the relationship of the market monitor in connection with ancillary services markets, and in particular, the energy imbalance market.

Alliance Cos., 94 FERC at 61,315 (footnote omitted, emphasis added).

Attachment G (at page 1) to the May 15 Compliance Filing sets out a "Description of Proposed Energy Imbalance Service for the Alliance RTO." The first sentence of that Description states that "[t]he Alliance RTO (ARTO) will provide Energy Imbalance Service under OATT Schedule 4 using a market-based approach." The Applicants go on to describe their proposal in very general terms, stating that "[t]he ARTO energy imbalance market will establish the imbalance energy price for each pricing zone for the energy provided and consumed for balancing service in each period." *Id.* at 2. While the Alliance Companies state "generators in one control area can supply imbalance energy to a different control area," congestion on the transmission system will result in differences in prices between zones. *Id.* The Alliance RTO will determine the imbalance prices to be used to pay for imbalance energy. "The ARTO designated price for the interval would be either the corresponding price bid for the energy by that generator or the corresponding Market Clearing Price of all bids submitted and accepted by the ARTO in the interval, as determined by the ARTO." *Id.* at 4.

Attachment G notes that “[t]he ARTO will be making a final determination of whether ‘pay-as-bid’ or ‘Market Clearing Price’ would be the most appropriate method [to compensate generators] for ‘instructed’ deviations for the imbalance market.” *Id.* Indeed, the decision as to which of these methods the Alliance RTO should use to price Day One Energy Imbalance Service has been a subject of much debate in the series of Market Development Advisory Group meetings held in Baltimore this spring. The Alliance TOs themselves are split on this issue, as are the attendees at the MDAG meetings, who were polled as to their preference.

The State Commissions are not opposed in principle to market-based pricing of generation supplied for ancillary services. If the proper competitive conditions are present, then this is likely the best and most efficient method to price the generation needed for the RTO to provide ancillary services. The State Commissions, however, do not believe that it is a rational, fact-based course simply to presume that there will be a competitive generation market to support the market pricing of such services, without any examination of whether the requisite competitive conditions in fact exist.

Attachment G is totally silent on the root issue underpinning market based pricing of Day One Energy Imbalance Service: whether there will be sufficient bidders and sufficient supply over a broad enough geographic market to ensure that the resulting market-based Energy Imbalance Service rates will be “just and reasonable” within the meaning of the Federal Power Act.⁷ Market-based pricing of generation-based ancillary services (be they provided by individual TOs or an RTO) should not be employed if market

⁷ “Departures from cost-based rates must be made, if at all, only when the non-cost factors are clearly identified and the substitute or supplemental ratemaking methods ensure that the resulting rate levels are justified by those factors.” *Farmers Union Central Exchange, Inc. v. FERC*, 734 F.2d 1486, 1530 (D.C. Cir.), *cert. denied*, 469 U.S. 1034 (1984). Accordingly, the Commission has approved market-based rate filings for wholesale electric sales based upon its express finding that such rates are or will be the result of competitive market forces and not the result of the seller’s exercise of market power to charge more than a competitive market price. *See Hermiston Generating Co.*, 72 FERC ¶ 61,071, at 61,351 (1995); *Citizens Power & Light Corp.*, 48 FERC ¶ 61,210, at 61,776-77 (1989).

conditions will not ensure that competition will act as a sufficient check on competitors to prevent the charging of excessive rates.

As a threshold legal matter, a third-party provider of ancillary services must be otherwise authorized to sell energy at market-based rates.⁸ However, having the authority to sell power at market-based rates does not automatically imply the authority to sell ancillary services at market-based rates, as the Commission concluded in establishing its ancillary services pricing principles in Order No. 888:

(2) The fact that we have authorized a utility to sell wholesale power at market-based rates does not mean we have authorized the utility to sell ancillary services at market-based rates.

(3) In the absence of a demonstration that the seller does not have market power in such services, rates for ancillary services should be cost-based and established as price caps . . .⁹

The Commission has insisted that the requisite demonstration of lack of market power must focus on the specific ancillary service markets. In *Ocean Vista Power Generation, L.L.C.*, 82 FERC ¶ 61,114 (1998), the Commission denied, without prejudice to refiling, requests for authority to

charge market-based rates for ancillary services, because the Applicants had not conducted an analysis of market power in the relevant ancillary services markets. The Commission concluded “[s]uch support must separately address the nature and characteristics of each ancillary service, as well as the nature and characteristics of generation capable of supplying each service, and must develop market shares for each service.” *Id.* at 61,407.

⁸ *Avista Corp.*, 87 FERC ¶ 61,223 at 61,880, n.1 (1999), *order on reh’g*, 89 FERC ¶ 61,136 (1999).

⁹ Order No. 888, FERC Stats. & Regs. ¶ 31,036 at 31,720 (1996); Order No. 888-A, FERC Stats. & Regs. ¶ 31,048 at 30,237-38 (1997).

In *Avista Corp.*, the Commission explained that the guidance offered in Order No. 888 and *Ocean Vista* “was designed for two purposes: to ensure that sellers of ancillary services do not exercise market power and to further the goal of promoting competition in ancillary service markets.”¹⁰ This policy has been followed by the Commission in subsequent orders granting authority for sales of ancillary services at market-based or “flexible” rates.¹¹

While market-based pricing of ancillary services has been used in ISOs formed using the platform of preexisting tight power pools (*e.g.*, PJM, NEPOOL),¹² Applicants acknowledge that they are starting from no such foundation. The Alliance RTO will be composed of a patchwork of individual transmission control areas that will continue for at least the next few years to be operated as individual transmission control areas. The Alliance Applicants themselves admit that “[t]his service is new to the historic service territories of the ARTO,” and that it is “a dramatic change in the way control areas are currently operated.” Attachment G at 1. Moreover, well-known transmission constraints internal to the Alliance TOs’ combined service territories may in fact result in *de facto* division of the RTO-wide energy imbalance market into a series of regional sub-markets when transmission constraints bind.

¹⁰ *Avista Corp.*, 87 FERC at 61,882 (third party ancillary service sellers that cannot perform a market power study are allowed to sell ancillary services at flexible rates, but only in conjunction with a requirement that such third parties establish an Internet-based OASIS-like site for providing information about and transacting ancillary services), *on reh’g*, 89 FERC ¶61,136 (1999) (clarifying that the requirement is for a web site that contains the specified information about ancillary services and sets forth procedures under which all customers would request service and make bids).

¹¹ *See, e.g., Wisconsin Electric Power Company*, 93 FERC ¶ 61,302 at 62,043 (2000) (holding that “consistent with *Avista*, we will authorize Wisconsin Electric to charge flexible rates for ancillary service provided it complies with the Internet-based site requirement . . .”).

¹² In approving NEPOOL’s proposal that the ISO procure certain ancillary services through bid-based markets, the Commission required a showing that there was no market power, noting: “Open, competitive markets may result in a more efficient procurement of ancillary services, to the benefit [sic] transmission customers. Indeed, there is only limited experience in the United States, mainly in California, with markets for ancillary service. This experience suggests that ancillary service markets are complex, and that initial market design may contain unintended flaws, especially as the ancillary service markets interact with energy and transmission markets.” *New England Power Pool*, 85 FERC ¶61,379 at 62,465 (1998), *reh’g denied*, 95 FERC ¶61,074 (2001).

Despite clear Commission precedent calling for a competitive market analysis¹³ and the Commission's explicit direction in its January 24 Order to "address concerns regarding the adequacy of competition in the market," *Alliance Cos.*, 94 FERC at 61,315, the May 15 Compliance Filing contains no discussion of the adequacy of competition in the Alliance RTO region to support market-pricing of Day One Energy Imbalance Service (or any other generation-based ancillary service). This omission is fatal.

A representative of one of the State Commissions joining in this protest, the Virginia State Corporation Commission ("VSCC"), raised this market power issue repeatedly at the series of MDAG meetings held this spring. The VSCC has questioned the wisdom of adopting either market-based method of pricing of Energy Imbalance Service (single price auction or pay-as-bid), in the absence of proof that bidding generators will not be able to exercise market power in the bidding process, gaming either set of market rules. At the most recent MDAG meeting held in Baltimore on June 5, 2001, the VSCC again raised this issue, and asked why the Alliance Companies had not addressed it in their May 15 Compliance Filing. The VSCC and the assembled participants were told by the Liaison from the Alliance Companies' RTO Management Committee that the market power issue was not an appropriate subject for discussion at the MDAG meetings, and that the Alliance Companies would address the issue in their August Tariff filing.

This continuing delay is not acceptable to the State Commissions, and should not be to the Commission. The Alliance Companies were told to address this issue in the January 24 Order, and had from then until May 15 to develop the necessary testimony and evidence to make the required showing on the competition issue. They chose not to do so. Now they have announced that this issue will not be addressed until their August tariff filing. This leaves only four months until Day One Energy Imbalance

¹³ See *Avista Corp.*, 87 FERC at 61,883, n.12 (noting that "our experience to date indicates that the data problems associated with market analysis involving sales to an ISO, for example, should not be insurmountable and an appropriate

Service is currently scheduled to commence to decide the most basic issue regarding that service – whether there is a sufficient competitive underpinning to support market pricing of it.

Moreover, the Alliance TOs reported at the June 5 MDAG meeting that the elements of the Day One Energy Imbalance Service had already effectively been decided (with the exception of the single price auction vs. as-billed issue) and the writing of the necessary software by the Alliance BridgeCo’s contractor, Siemens, is now well underway. In July, the software is scheduled to be in the testing phase. Thus, by August, the Alliance Companies may well assert that changing any essential element of the RTO’s Day One Energy Imbalance Service Pricing would require rewriting of the software, potentially delaying the Alliance RTO’s start-up date.

This situation would not be acceptable even if the Alliance TOs had no commercial interest in this issue. But many of the Alliance TOs own substantial generation facilities in their transmission service territories, and some are the dominant generators in their service territories. Thus, if market-pricing of Day One Energy Imbalance Service and other RTO generation-based ancillary services were to be permitted, they would stand to gain financially from any supra-competitive auction prices they obtained for their generation under the energy imbalance service auction rules they set up for the Alliance RTO. The fact that this is so, and that the software protocols for the RTO’s Day One Energy Imbalance Service are being written under their supervision even as this protest is being filed, should be cause for grave concern.¹⁴

showing of lack of market power can be made”).

¹⁴ See *GridFlorida LLC*, 94 FERC ¶ 61,363 at 62,325 (2001) (explaining that “[t]he Commission regards the acquisition of software and other systems implementing market design as significant to the future operation of the RTO and will require that any acquisition of software or other systems implementing market design not be undertaken until the independent Board has been seated and given its approval.”).

2. Other Ancillary Services.

The bulk of the discussion regarding this issue has to date taken place in the context of Day One Energy Imbalance Service, because that is the only generation-based ancillary service discussed in any detail in the May 15 Compliance Filing. It has also been the primary service offering discussed to date in the MDAG meetings, although that Group will now be moving to Day Two¹⁵ discussions. In fact, Day One Energy Imbalance Service is only one aspect of the larger issue of market-based ancillary service pricing. The RTO will handle congestion management on Day One by obtaining mandatory incremental and decremental bids from generators. Assuming that those bids are non-cost based, then the same competitive concerns arise, *i.e.*, will the Alliance RTO be required to pay supra-competitive prices to clear congestion on the system? Day Two energy imbalance and congestion clearance mechanisms promise to be even more complex (with congestion being dealt with using a “hybrid” flowgate/LMP regime). All of these methodologies presume as a fundamental underpinning a competitive market for generation.

In sum, intervenors have previously raised competitive concerns about the pricing of the RTO’s ancillary services, and the Commission has directed the Applicants to address them. The Applicants should be required to comply with the Commission’s directive immediately, rather than deferring Commission consideration of this issue until the time that it reviews the Alliance Companies’ August tariff filing.

C. OASIS and Total Transmission Capability

The January 24 Order directed the Alliance Companies to file the system of tests and checks to be used by Alliance. *Alliance Cos.*, 94 FERC at 61,316. Attachment H of the May 15 Filing contains Revisions to Section 3.1.1 of the Operating Protocol, to clarify that any data supplied by others to calculate

¹⁵ “Day Two” is the term the Alliance Companies use to refer to the date upon which fully market-based energy imbalance and congestion management mechanisms will be put in place.

ATC will be “coordinated and unbiased.” The adequacy of this still very generalized response is contingent on proper implementation of the IRCA, about which the May 15 Filing says very little.

D. Rate Issues

1. Administrative Fee: The Alliance Companies were directed to support their methodology with detailed cost support that will allow verification of their results when they file their actual rates.

Alliance Cos., 94 FERC at 61,320.

2. Loss Methodology: The January 24 Order found that the Alliance Companies’ proposed loss methodology is unclear. Specifically, the Alliance Companies: (1) did not support the necessity of rounding schedules up to the next whole MW; (2) failed to demonstrate that the cumulative approach to determining losses for multi-zone transactions is reasonable; and (3) did not account for holidays. *Id.* at 61,321.

3. Failure to Curtail Penalty: The Alliance Companies initially proposed to charge a \$50/kW penalty for failure to curtail pursuant to the transmission provider’s directive. *Id.* at 61,322. The Commission directed the Alliance Companies to delete the penalty or propose a new penalty that is consistent with Commission precedent on penalties. If the Alliance Companies included a new penalty, they were required to explicitly delineate the response times and actions required of customers at the time of curtailment prior to imposing a penalty for failure to curtail. *Id.*

In their May 15 Filing, the Alliance Companies address none of these or any other rate issues. They state that any matters not addressed will be addressed in a filing or filings submitted no later than 120 days before the Alliance RTO transmission service date. Matters not yet addressed include the Alliance RTO OATT, support for proposed rates and a long-term congestion plan.

This plan is not consistent with the January 24 Order, which required the compliance filing to demonstrate compliance. Moreover, the adequacy of the Alliance Companies' assurance that these matters will be adequately addressed in the future hinges on the existence of an adequate stakeholder process, which, as discussed *supra*, does not exist.

E. Non-Rate Terms and Conditions

1. Modifications on a Non-Firm Basis: Alliance Companies were directed to require that requests for non-firm point-to-point service over secondary receipt and delivery points in amounts not to exceed firm reservation be made on OASIS. *Id.* at 61,323.

2. Network Transmission Service: Alliance Companies were directed to delete the reference to firm sales under Section 30.4 of the Alliance OATT. *Id.* at 61,323-24.

3. Sequential Off-Peak Hourly Service: Alliance Companies were directed to include the provision that such service is consistent with the pro forma tariff, so long as the bumping provisions were not upset in their section 14.2 of the OATT which contains the non-firm priority provisions. *Id.* at 61,324-25.

Again, the Compliance Filing addresses none of these issues, apparently with the intent of delaying them until the August tariff filing.

F. The Process for Acquiring Goods and Services Remains Uncorrected

FERC's January 24 Order stated:

Alliance Companies agree that Alliance Publico should be required to take the "best" bid to provide goods or services, based on objective criteria, whether or not such a bid is submitted by a Class B or Class C interest holder. Alliance Companies indicate that this issue will be addressed further in their executed final agreements which must be submitted as part of their compliance filing, and we will defer further consideration of this issue until that filing.

Alliance Cos., 94 FERC at 61,304-305 (footnote omitted).

There still is nothing for the Commission to consider, because in their May 15 Compliance Filing, the Alliance Companies submitted no “executed final agreements.” This unexplained omission, of a feature essential for independence, is further evidence that the road to independence remains long and uncertain.

G. The Independence Audit Process Remains Incomplete

The Commission’s January 24 Order stated:

Attachment K also provides for independence audits. In our Alliance II Order, we stated that “the Alliance Companies should address, with respect to their proposed transco, our Order No. 2000 independence audit requirement.” Alliance Companies have proposed to chronologically schedule those independence audits consistent with the Commission’s requirements but have offered no additional details about the audits themselves beyond that provided in their last filing. Alliance Companies should clarify that the independence audit requirement applies to both Alliance Transco and Alliance Publico.

Id. at 61,305 (footnote omitted). The Alliance Companies’ only action on the independence audit issue was to add this sentence (*see* May 15 Filing (Attachment D, Section 7.5)):

The audits must evaluate whether the Company and the Managing Member are independent of Market Participants.

The Commission’s May 8 Order provides further guidance regarding the independence audit process:

[W]e clarify that we expect that an independence auditor will be able to conduct audits with adequate depth to actually determine whether the RTO is independent of market participants, and that such an audit will be based on full auditor access to all information the auditor deems necessary and relevant to its inquiry. When the independence audit is submitted to the Commission, all parties will have the right to examine it, and to raise any questions they may have about the resources of, the methodology used by, and the outside relationships of, the auditor.

Alliance Cos., 95 FERC at 61,624-25.

The Commission should direct the Alliance Companies to file a detailed protocol for the independence audits that assures that an independence auditor has sufficient access to necessary information for determining whether the Alliance Transco, Alliance Publico or any interim managing entity are truly independent of market participants. It is critically important that the Commission require that an independence auditor have all of the necessary tools for conducting comprehensive examinations of market independence, including a sufficient budget. All employees of the Company, the Managing Member and the Class B/C unit holders should be made available to the auditor for interviews, and the confidentiality of those interviews should be guaranteed.

Additionally, to ensure that the audits truly do what the Alliance Companies' inserted language purports to do (*i.e.*, "evaluate whether the Company and the Managing Member are independent of Market Participants"), it is insufficient to state that the auditor may not be an "Affiliate of the Company," a "Member of the Company" or a "Non-Divesting Transmission Owner." Rather, Section 7.5 should be further amended to clarify that the auditor may not have any business relationship with or any financial ties to an "Affiliate of the Company," a "Member of the Company" or a "Non-Divesting Transmission Owner." If, for example, the RTO were to hire as its "independence" auditor a firm which is not a Transmission Owner, but which conducts audits for one of the Transmission Owners, the independence of that auditor is dubious. Such an auditor may think twice about making a finding that the Company and Managing Member are not independent of Market Participants if it fears it would lose substantial business from its employer, the same Transmission Owner about which it is supposed to be making an unbiased audit and determination of independence.

IV. The Compliance Filing Reflects Insufficient Progress on Congestion Management and

Other Indicia of Capability Building

The May 15 Filing provides little comfort that the Alliance RTO will be prepared to operate as of December 15, 2001. So little progress has been made in so many critical areas as to raise considerable doubt about Day 1 operational capability. So little progress is being made in other areas as to leave the conviction that, even if the RTO can physically operate, it will not be prepared to perform required RTO functions and duties.

One example is transmission planning. While Order No. 2000 permits an RTO to seek additional time to implement a transmission planning system, an RTO does not automatically get an extension and the Alliance Companies have not asked for one. The Alliance Companies have included an elaborate transmission planning protocol in the September 15 filing (Attachment H), which was slightly modified in the May 15 filing (Attachment I). The protocol involves the establishment of committees and the development of regional transmission planning capability. However, the State Commissions are aware of no efforts that would assure that these planning functions and capability can be in place anytime soon. No committees have been formed. The necessary software has not been installed. In short, the Alliance Companies have an elaborate plan, but no means to make it functional. At this late stage in the RTO development process, the Alliance Companies must be able to show more than words on paper. It will take some time to build the capability to conduct meaningful regional transmission planning. The Alliance Companies' May 15 filing purports to "supplement" earlier Alliance Companies' RTO filings. It is not unreasonable to expect that such filings demonstrate the steps being taken to actually implement proposals such as the transmission planning protocol that are so important to obtaining the goals of Order 2000. Although these functions may not be required for Day 1 physical operations, they are much of the reason for having an RTO in the first place. The Commission should direct the Alliance Companies to take immediate steps to move the

protocols from paper to practice, including establishment of the Planning Advisory Subcommittee called for in Section 5.3.5 of the IRCA.

Another example is congestion management. The generation-owning utilities that currently run the Alliance RTO notified the MISO of their intent to defer consideration of long-term congestion management due to the asserted need to address more immediate issues. This notification conflicts with Section 4.2.3 of the Inter-RTO Cooperation Agreement, requiring that “procedures and protocols” for long-term congestion management between the Alliance RTO and the MISO be completed by December 31, 2001.

The Alliance Companies’ decision to delay coordination efforts for long-term congestion management has both short-run and long-run consequences, all adverse, for the efficient and reliable operation of a broad regional market. Moreover, there is a disturbing pattern emerging that the Alliance Companies are incapable of making difficult decisions in a timely manner, and, as a result, the Alliance Companies appear to look for quick fixes that are incompatible with a single regional market. Failure to resolve fundamental operational and policy issues, within the Alliance RTO, will frustrate inter-RTO coordination and foster inefficiencies as well as the attendant costs.

The Alliance Companies have recently stated their intention to have at least three Security Coordinators, with the attendant costs and inefficiencies (e.g., the MISO was told by the Alliance Companies that they would not consider any MISO proposal even if it were a lower cost than any competing proposal). Because the effectiveness of any congestion management protocol is inextricably intertwined with the actions of the Security Coordinator, we are deeply concerned that the Alliance RTO proposal for three (or more) Security Coordinators could diminish the effectiveness of congestion management to reduce the need for issuing TLRs. A multiplicity of Security Coordinators, when one or two

should suffice, could also contribute to a decline in reliability if communications with other security coordinators are inefficient or if there are differences in calculating ATC and protocols for issuing TLRs. These differences in calculating ATC or issuing TLRs could result in undue market advantages for the utility-Security Coordinators. If there are perceived or actual market advantages, it is possible that this will spur a proliferation of Security Coordinators.

In the short-term, inconsistent congestion management approaches among the PJM, MISO, and the Alliance RTO will frustrate achievement of the “seamless” regional market at best; the more likely scenario is serious reliability problems. The lack of discernable progress on other critical and interrelated matters, such as the real-time balancing market, heighten our concern.

For the long-term, it is imperative that there be a single regional approach to congestion management in the Midwest. A year or two ago, experimentation with various congestion management approaches had some merit and stirred some interesting academic discussions. The time for experimentation has expired, however, and must give way to the need to have a consistent regional approach to congestion management. Even in the best case, it is truly unfortunate to spend money on a “Day 1” solution that will largely be wasted as soon as the “Day 2” approach becomes operational. Anything the RTOs can implement from Day 2 congestion management on Day 1 will make the transition easier.

The Alliance Companies’ postponement of a long-term approach to congestion management is indicative of the systemic organizational problems within the Alliance RTO. The failure of the utility owners of the Alliance RTO to develop a long-term congestion management approach, notwithstanding months of time during which they were hardly disturbed by stakeholder input, at best reflects their inability to resolve fundamental issues and cooperate in a joint process; at worst represents delay aimed at protecting the

Companies' generation market shares. We have no confidence that the current decision making processes of the Alliance RTO will ever result in a harmonious regional approach to congestion management.

The same companies' failure to establish a congestion management protocol also raises serious questions regarding the Alliance RTO's ability to develop an efficient real-time balancing market, and the ability to provide ancillary services which are necessary to an efficient and seamless regional market.

For these reasons, the State Commissions urge the Commission to order the Alliance Companies to use the expertise and insights of the various stakeholders to help resolve implementation issues and to actively work with the MISO to coordinate important operational functions so as to remove any unnecessary impediments to a broad and efficient regional power market for the short and the long-term.

CONCLUSION

WHEREFORE, for the foregoing reasons, the State Commissions urge the Commission to give specific direction and establish specific deadlines, as set forth in this document.

Respectfully submitted,

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Dated: June 18, 2001

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CERTIFICATE OF SERVICE

I hereby certify that I have this day served a copy of the foregoing document by first-class mail upon each party on the official service list compiled by the Secretary in these proceedings.

Dated at Washington, D.C., this 18th day of June, 2001.

Phyllis G. Kimmel

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